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SUBJECT: ROUND TABLE REVEALS STRENGTHS, WEAKNESSES IN RUSSIA'S SMALL BUSINESS SECTOR

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¶1. (U) On January 20, Consul General attended a round table on small and medium enterprise (SME) in Nizhniy Tagil, 180 km north of Yekaterinburg. The event was organized by the Sverdlovsk Oblast government and hosted by the recently elected maverick mayor of Nizhniy Tagil, Valentina Isayeva (see reftel). Counting the CG, about a dozen representatives of Yekaterinburg's diplomatic missions attended. In brief remarks to the group, the CG outlined steps the U.S. government had taken to address the financial crisis and discussed how measures and policies put forth by President Obama support small business.

¶2. (U) The industrial center of Nizhniy Tagil is the second largest city in Sverdlovsk Oblast with a population of over 375,000. Such internationally known giants as Nizhniy Tagil Metallurgical Combine and Uralvagonzavod, which manufactures the T-90S and T-72S tanks and various types of railway tankers and carriages, are major employers. Large industrial enterprises provide over 95 percent of the industrial output in the city. A small, but significant SME sector arose during the 1990s economic reform. According to official figures, the city is home to 3,600 small and medium enterprises that provide jobs for about 37,000 people.

¶3. (U) Local officials gave presentations on the availability of business consulting and promotion services. They expressed interest in attracting investors in solid waste processing (including waste recycling), logistics, food processing and public transportation. They acknowledged, however, that a number of problems still plague the sector, including: complex business registration procedures; high cost and lack of available credit; poorly developed business real estate sector; undeveloped leasing sector; and lack of cooperation between large and small businesses.

¶4. (U) Despite these problems, we heard relatively optimistic presentations from a half dozen or so entrepreneurs in manufacturing, furniture-making, and food processing. Though no statistics on the success/failure rate of small businesses were made available, we noted that three of the companies that made presentations provided products or services to the troubled heavy industry sector. Still, most of the presenters were seeking new technology and equipment and it was clear they were not terminating their business development plans.

¶5. (SBU) On a regional level, according to media reports, Sverdlovsk Oblast has allocated RR 250 million (about US\$ 7.5 million) to support of SMEs in 2009. But local businessmen view these government programs as ineffective. According to one observer, when a similar strategy to support small business was implemented in the 1990s, much of the money was spent on administrative overhead or otherwise expended before reaching the target businesses. In a recent conversation, a successful local businessman characterized as inadequate government efforts to address the issues of administrative barriers, favoritism in awarding government contracts, a burdensome and complex tax system, and lack of credit that plague the sector today. He also criticized Delovaya Rossiya, a national business

association that was established to support small and medium business, for what he called its overly bureaucratic approach. He commented that he was fortunate that his company had no debt.

Though he has had to lay off some workers, he was confident that his business, which is seasonal, would rebound with the resumption of construction projects in the spring.

16. (SBU) Comment: Though local governments are allocating resources and expressing support for SMEs, their efforts may not be enough to overcome the administrative and structural barriers that currently exist, and that are being exacerbated by the Russia's financial crisis. Companies that are free from debt and not tied to heavy industry are likely to emerge from the crisis in the best shape. But in difficult economic times, the toll on small business is great, and it remains to be seen whether the mutual expectations of business and government will be met as the crisis deepens.

SANDUSKY